STATE BOARD OF LAND COMMISSIONERS
SPECIAL MEETING
Regular Agenda
June 22, 2000

SUBJECT

Variable Spending Policy and General Policy Guidelines

BACKGROUND

The Variable Spending Policy (VSP) and general policy guidelines were developed for the Endowment Fund Investment Board by the QInsight Group for fiscal year 2001 in response to the Investment Reform Committee's request that the EFIB develop the policies and procedures to implement investment reform. After careful consideration of the VSP, the Endowment Fund Investment Board accepted QInsight's recommended spending policies. We now request that the Board of Land Commissioners approve these policies to become effective July 1, 2000.

DISCUSSION

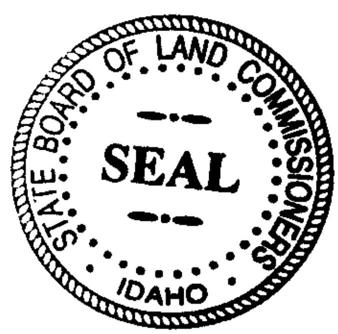
The VSP provides a way to invest the permanent endowment fund to get the highest return for the least risk. It also provides for present and future payments to beneficiaries with the added assurance that the Endowment Corpus will continue to grow as the population grows and when inflation increases.

RECOMMENDATION

The Endowment Fund Investment Board recommends that the Board of Land Commissioners review the attached Variable Spending Policy as preparation for approval at the Special Board of Land Commissioners meeting on June 22, 2000.

BOARD ACTION

APPROVED JUN 2 2 2000



ATTACHMENT

Variable Spending Policy and Investment Policy Guidelines

VARIABLE SPENDING POLICY
Developed by The QInsight Group for the Endowment Fund Investment Board

The objectives of this spending policy are as follows:

A. **To maintain the purchasing power of the Permanent Endowment Funds** - The Endowment Corpus Funds are required to grow at an annual rate equal to a three (3) year moving average of a Composite Index computed as the sum of a general inflation index and an annual population growth rate.

B. **To maintain fair and equitable inter-generational funding** - The Spending Rule for current beneficiaries is set at a level and growth rate that can be maintained for an extended period of time without jeopardizing the long-term growth required in the permanent endowment funds. The Spending Rule is based on a three (3) year moving average of the market value of the endowment corpus funds.

C. **To achieve smooth and predictable spending** - A Stabilization Fund is established at a level designed to maintain a relatively constant growth rate of the annual distributions to the beneficiaries.

D. **To maintain a constant ratio between the Endowment Corpus Funds and the Stabilization Funds** - The Stabilization Funds shall be funded to a level that provides for the required growth in the Endowment Corpus Funds and the beneficiary distributions.

Structure

The Idaho Endowment Fund structure is described in terms of a funds flow diagram (figure below). The diagram is a visual model illustrating how the endowment funds will flow through the system when the reform endowment trust legislation takes effect in July 2000. The diagram is best interpreted from left to right and top to bottom, beginning with the sources of funds on the top left side of the diagram, proceeding with the management of the funds in the center, and distribution of the funds on the right hand side. Key terms such as "Stabilization Fund" are defined below.

Terms and Definitions

The key endowment terms and definitions are presented below. They are defined in operational and procedural terms in order to allow the reader to understand how they are applied and used in the following subsections, which describe each of the specific VSP Project endowment polices.

A. **Endowment Corpus Funds and Endowment Unrealized Funds** - The Endowment Funds are permanent funds and are to be invested for the purpose of generating future income. These funds are not permitted to be used for current spending. Earnings from the

Endowment Funds are to be deposited in the Earnings Reserve Funds. It is the policy of the Endowment Fund Investment Board that the Endowment Funds shall be further divided into Endowment Corpus Funds and Endowment Unrealized Funds internal balances.

- The Endowment Corpus Funds are defined at the end of each accounting year to be the following: Endowment Corpus Funds (at the previous accounting year-end) multiplied by the Composite Index growth rate (consisting of the general inflation index plus the product of the general inflation index and the population growth index).

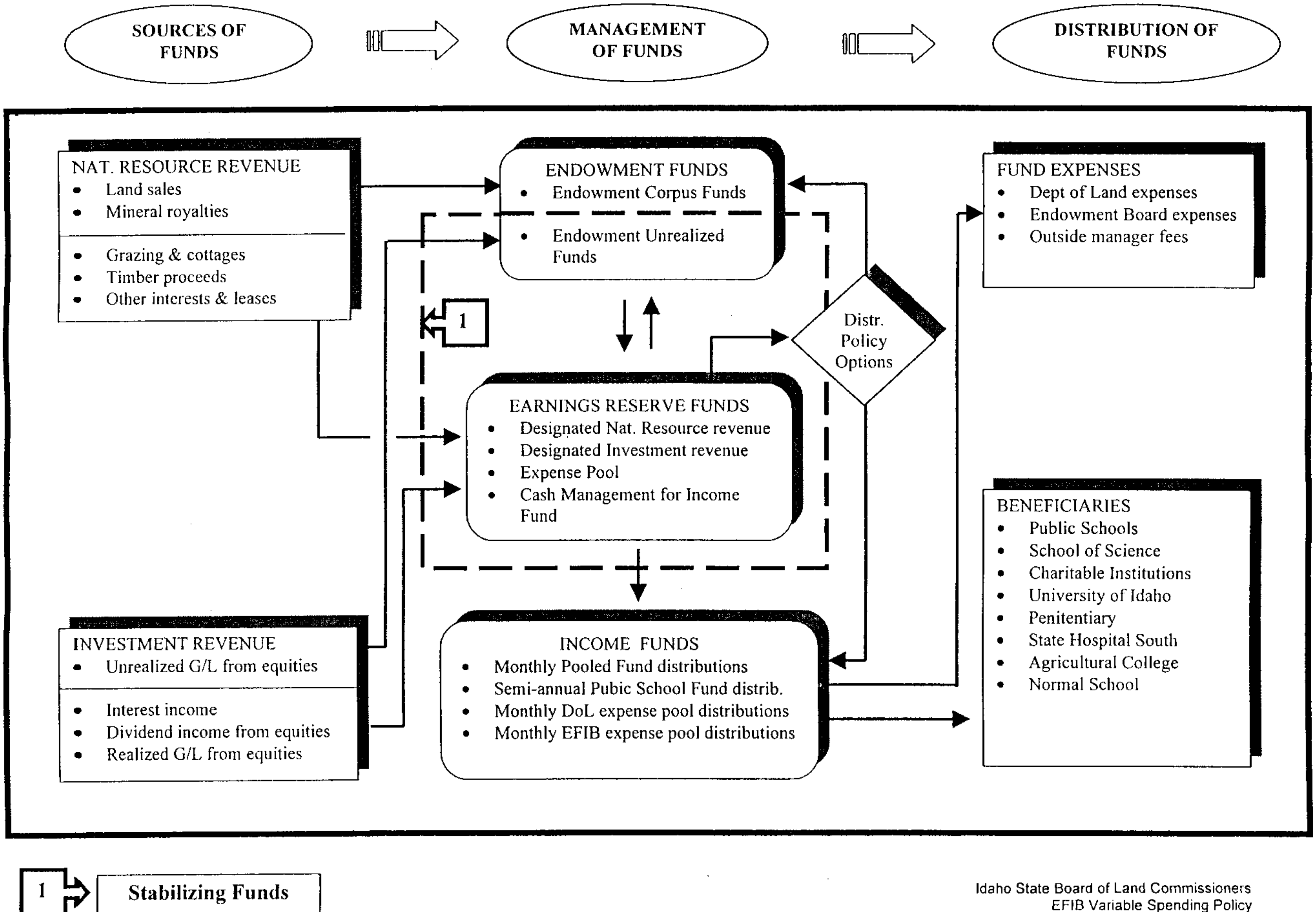
- The Endowment Unrealized Funds shall be the remaining Endowment Funds that are not realized. The Endowment Unrealized Funds are defined as part of the Stabilization Funds (along with the Earnings Reserve Funds) since the Endowment Unrealized Funds will be transferred to the Earnings Reserve Funds as soon as sufficient unrealized earnings are converted to net realized earnings.

B. **Earnings** - Earnings are defined to be all revenues from the management of the Endowment Lands and the Endowment Funds including timber sale proceeds, lease fees, interest, dividends and net realized capital gains. Earnings do not include mineral royalties or land sale proceeds that are deposited directly in the Endowment Funds or net unrealized capital gains that remain in the Endowment Funds until realized.

C. **Earnings Reserve Funds** - The Earnings Reserve Funds consist of the accumulated earnings distributed from the Endowment Lands or the Endowment Funds, plus dividends, interest, and realized or unrealized gains on previous earnings reserve balances. All Endowment Land earnings will be deposited directly in the Earnings Reserve Funds and all revenues earned in the Endowment Funds will be transferred into the Earnings Reserve Funds at least every six months. The administrative expenses of the Endowment Fund Investment Board, the Department of Lands and the management fees for all the funds will be appropriated from the Earnings Reserve Funds.

D. **Stabilization Funds** - The Stabilization Funds are used to stabilize both the long-term growth of the Endowment Funds and the annual beneficiary distributions. The Stabilization Funds consist of the Earnings Reserve Funds and the Endowment Unrealized Funds.

E. **Income Funds** - The Income Funds consist of the distributions required to be made to the beneficiaries and the operating expenses to be paid for the Department of Lands and the Endowment Fund Investment Board. The Income Funds also include any interest or dividends earned on these funds. The beneficiary distributions are subject to legislative appropriation and approval. The interest and dividends earned on the Department of Lands and the Endowment Fund Investment Board's Income Funds will be transferred into their respective Earnings Reserve Funds. The interest and dividends earned on the beneficiary Income Funds belong to the beneficiaries and will be paid out to them.


SOURCES OF FUNDS
MANAGEMENT OF FUNDS
DISTRIBUTION OF FUNDS
NAT. RESOURCE REVENUE
• Land sales
• Mineral royalties
• Grazing & cottages
• Timber proceeds
• Other interests & leases
ENDOWMENT FUNDS
• Endowment Corpus Funds
• Endowment Unrealized Funds
1
Distr. Policy Options
EARNINGS RESERVE FUNDS
• Designated Nat. Resource revenue
• Designated Investment revenue
• Expense Pool
• Cash Management for Income Fund
FUND EXPENSES
• Dept of Land expenses
• Endowment Board expenses
• Outside manager fees
BENEFICIARIES
• Public Schools
• School of Science
• Charitable Institutions
• University of Idaho
• Penitentiary
• State Hospital South
• Agricultural College
• Normal School
INVESTMENT REVENUE
• Unrealized G/L from equities
• Interest income
• Dividend income from equities
• Realized G/L from equities
INCOME FUNDS
• Monthly Pooled Fund distributions
• Semi-annual Pubic School Fund distrib.
• Monthly DoL expense pool distributions
• Monthly EFIB expense pool distributions
1
Stabilizing Funds

F. **Threshold Level** - The Stabilization Funds are to provide sufficient funds to sustain both the beneficiaries' distributions and the purchasing power of the Endowment Funds. Based on a historic simulation of the US capital markets from 1960 to 1998, it has been determined that the Stabilization Funds require a funding level equal to 50% of the respective Endowment Corpus Fund. See the *Funding Priority* sub-section for a discussion of the policy decisions to be made once the Threshold Level has been achieved.

G. **Composite Index** - This is the required annual growth rate for the Endowment Corpus Funds. It is the three (3) year moving average of the product of the consumer price index and the Idaho population growth rate.

Annual Reviews

The Spending Rule and the combined funds' (i.e. the Endowment Funds and the Stabilization Funds) asset allocation will be reviewed at least annually using the Simulation Model and the Sources & Uses Model. The Sources & Uses Model combines the budgetary and funding requirements for the beneficiary entities and the revenue and departmental expenses for the Department of Lands and the Endowment Fund Investment Board. The Simulation Model combines the beneficiary funding requirements and forecasted revenues from the Sources & Uses Model with the forecasted earnings from the combined funds to prepare a comprehensive, annual spending policy review.

Initial Spending Rule

The initial Spending Rule (annual percentage) will be reviewed and approved annually by the Endowment Fund Investment Board. The amount available for current distribution to the beneficiaries is determined by multiplying the Spending Rule times a three (3) year moving average of the Endowment Corpus. The purpose of the three (3) year moving average is to smooth the annual distributions to the beneficiaries.

- The initial Spending Rule is approved at 8.50% based on the goal of meeting the current spending objectives established for the endowment fund and its beneficiary organizations. It also permits the early accumulation of the Stabilization Funds to the required Threshold Level.

- It is anticipated that the initial Spending Rule will not change until after the Stabilization Funds have exceeded the Threshold Level, at which time the Endowment Fund Investment Board may decide to change the Spending Rule. See the *Variable Spending Rule* sub-section below for a summary of the alternatives the Endowment Fund Investment Board may consider after the Threshold Level has been attained.

Funding Priorities

Each year, the first priority of the Stabilization Funds is to completely or partially, if required, the annual distributions to the beneficiaries. The next priority for the Stabilization Funds is to completely or partially fund, if required, the annual increase in purchasing power for the Endowment Corpus Funds.

In the event the Endowment Corpus Funds do not grow (in any year) at an annual rate equal to or greater than the required Composite Index growth rate (i.e. the general inflation rate plus the general population growth rate), and the Stabilization Funds have fulfilled the first priority described above, then the additional amount required to bring the Endowment Corpus Funds to their required level will be transferred from the Stabilization Funds to the Endowment Corpus Funds. In the event the level of the Stabilization Funds is insufficient to fund the annual increase required by the Endowment Corpus Funds, the amount of the unfunded contribution will be deferred to the next year and will be added to the next year's required contribution to the Endowment Corpus Funds. All deferred, required contributions to Endowment Corpus Funds are cumulative without limit. The cumulative deferred contributions to Endowment Corpus Funds do not have to be funded from the Stabilization Funds in a single year, but must be funded as soon as is fiscally responsible.

In the event the level of the Stabilization Funds is insufficient to fund the annual beneficiary distributions, the amount of the unfunded distributions will be deferred to the next year and will be added to the next year's required distributions. All deferred, required distributions are cumulative without limit. The cumulative deferred distributions do not have to be funded from the Stabilization Funds in a single year, but must be funded as soon as is fiscally responsible.

Deferred beneficiary distributions have priority on any available Stabilization Funds over deferred contributions to the Endowment Funds.

Future Variable Spending Rule Alternatives

Once the Stabilization Fund has met or exceeded the Threshold Level, the Endowment Fund Investment Board (EFIB) may consider any one or a combination of three alternatives: modify (increase) the Spending Rule, approve one-time special distributions or increase the contribution to the Endowment Fund (and a matching 50% contribution to the Stabilization Funds) above the required Composite Index growth rate. In general, it is anticipated that the Spending Rule will be increased. In the event the Stabilization Funds subsequently fall below the Threshold Level, a new Spending Rule will be established by the Endowment Fund Investment Board based on an updated review of the VSP Simulation Model.

GENERAL INVESTMENT POLICY

This Investment Policy Statement is set forth so that:

A: The Endowment Fund Investment Board (EFIB) and its Advisors, Consultants and Investment Managers will have a clear understanding of the investment objectives, policies, and guidelines so as to limit the chance of a misunderstanding.

B: Each Advisor, Consultant and Investment Manager for the Endowment Fund's assets will understand the guidelines, limitations and directives in investing these assets. These guidelines and limitations are meant to be sufficiently specific to be meaningful, but flexible enough to be practical.

C. The Endowment Fund Investment Board will have a meaningful basis for reviewing and evaluating each Advisor's, Consultant's or Investment Manager's progress in meeting the EFIB's investment objectives.

Objectives

This Investment Policy Statement is issued by the Endowment Fund Investment Board (EFIB) for the guidance of its Consultants, Advisors and Investment Managers in the investment of the Endowment Fund assets. The objectives for the Endowment Fund are listed in the *Objectives* section of the Spending Policy. The overall management objective for the Endowment Fund assets is to preserve the real, per capita purchasing power of the Endowment Corpus Funds while providing a long-term sustainable level of beneficiary distributions.

A. The Endowment Fund's assets are maintained primarily to provide for the current and future beneficiary distributions. The EFIB's Spending Policy assumes that annual spending will average 8.50% of a three (3) year moving average of the market value of the Endowment Corpus Funds. These annual distributions will generally come from the Earnings Reserve Funds' earnings and the Department of Land's revenues. Therefore, the Endowment Fund equity assets are anticipated to be committed for an investment time horizon of at least five years. From time to time, however, it may be necessary to use capital gains funds to make beneficiary distributions and to transfer balances from the Endowment Unrealized Funds to the Earnings Reserve Funds. Therefore, each Investment Manager is required to meet the liquidity requirements listed in Section 3.3, *General Investment Guidelines* and in the specific guidelines for each Investment Manager and to be aware that the EFIB may require the Investment Manager to convert unrealized net gains into realized net gains from time to time.

B. The EFIB seeks both preservation of capital and growth of capital on a real return basis. Growth of capital means that while short-term fluctuations may, on occasion, result in the loss of capital, the EFIB expects asset growth (exclusive of contributions or withdrawals) over the investment time horizon to achieve the objectives listed in this document. Preservation of capital means that capital gains are to be protected over the investment time horizon. The EFIB does not wish to take significant risks with their assets, and they are more concerned with minimizing losses than maximizing gains. The EFIB wishes to out-perform the general markets on a relative basis during periods of negative returns in the general market.

C. Based on a historical analysis, the EFIB has chosen an initial conservative long-term asset allocation policy of 70% equities, 30% fixed income. This is a decision to remain conservative during the initial periods of the new investment policies until the required Stabilization Funds have accumulated. Further, the EFIB has chosen the S&P 500 index as the target index for the equity portion of the portfolio and the Lehman Intermediate Government/Corporate index as the target index for the fixed income portion of the portfolio. Based on this asset allocation the EFIB wishes to achieve the following objectives after all expenses:

	Equities	**Fixed Income**	**Combined**
Nominal Annual Return	10.30%	7.40%	9.40%
Real Annual Returns	5.30%	2.40%	4.40%
Standard Deviation (annual)	15.90%	7.40%	12.90%
Probability that Annual Returns are less than 0.	Not applicable	Not applicable	22%

General Investment Guidelines

The following represent general Investment Policy guidelines:

A. The following ranges are recommended for the major asset classes:

Asset Category:	**Minimum**	**Maximum**	**Target**
Equities	40%	80%	70%
Fixed Income	20%	60%	30%

B. The Endowment Fund Investment Board does not intend to use market timing as an investment policy. However, the investment policy should provide the flexibility for tactical asset allocation using capitalization, investment styles, sectors and other factors.

C. Both the Endowment Funds and the Earnings Reserve Funds are long-term investments. Therefore, it is important that these funds be reviewed for re-balancing to the targeted asset allocation at least twice a year with an annual rebalancing. The need to re-balance the funds adds definite liquidity requirements to all the securities purchased by the Investment Managers:

- All securities must have readily ascertainable market values and be easily marketed.

- All securities must have adequate market liquidity relative to the size of the investment.

- The Investment Managers for the small- and mid-capitalization equity asset classes may have difficulty complying with these liquidity requirements as they may own a substantial percentage of the outstanding shares of a corporation or they may own shares that are "thinly-traded."

D. In order to reduce the portfolio's volatility in periods of higher than average inflation, the asset allocation guidelines include an "inflation trigger" that reduces the total equity allocation and increases the allocation to intermediate fixed-income (with a 6-month lag) when the annual inflation rate exceeds 5.5%. When the annual inflation rate drops below its twelve (12) month simple moving average, the "inflation trigger" policy is reversed. At that time the Funds' allocation to stocks is increased and the allocation to intermediate-term fixed-income is decreased.he 5.5% annual rate was selected on the basis of a cumulative distribution analysis of the 1960 to 1998 period that shows the annual inflation rate rose above 5.5% less than 33% of the time.

E. Cash reserves should be invested in interest bearing securities.

F. Investments should be prudently selected and properly diversified consistent with the risk tolerance and investment objectives of the EFIB.

G. The duration of the fixed income portion of the EFIB funds shall remain as close to the duration of the Lehman Intermediate Government/Corporate index as is possible.

H. Individual Investment Manager guidelines will be provided to each Investment Manager by the EFIB. These guidelines are considered part of the Investment Policy Statement. The specific liquidity requirements should be included in the investment guidelines for each Investment Manager.

Allowed Investments

The following is a list of asset classes allowed by this Investment Policy:

A. Domestic equities include the following categories:
   - Large-capitalization domestic stocks include core, value and growth style categories.
   - Mid-capitalization domestic stocks include core, value and growth style categories.

B. Small-capitalization domestic stocks include core, value and growth style categories.

Note: The capitalization definitions may be defined by the Standard & Poors, Russell, Wilshire or any other definition deemed appropriate by the EFIB.

C. International equities (i.e., shares of companies denominated in non-US currencies and depository receipts traded in the US) include

- Small- and large-capitalization classes
- Super-regional geographic areas such as Europe, the Pacific region, etc., and developed and emerging markets.

Note: Investments in the countries included in the Morgan Stanley Capital International Europe, Australia, and the Far East index (EAFE) will be no less than 90% of the international equity portfolio. No more than 10% of the international equity portfolio may be in equities in non-EAFE countries.

D. Fixed income securities included in the Lehman Intermediate Government/Corporate Index are allowed, including the following:

- US Government and Agency securities (notes, bonds and other instruments) include short, intermediate and long-term maturity categories. The fixed income portfolio is intended to be a high quality portfolio. All domestic corporate bonds, notes, debentures or convertible debt securities must have a minimum "BBB" rating by Standard & Poors or a "Baa3" rating by Moody's (or equivalent ratings by other national rating services).

- Yankee bonds are allowable securities and must have a minimum "A" rating by one of the national rating services, and are limited to five percent (5%) of the market value of the fixed income portion of the total portfolio.

- Commercial paper is limited to 5% of the fixed income portfolio.

- Equity-linked debt must have a minimum rating of A by a national rating service, and are limited to five percent (5%) of total book value of their respective portfolios.

E. In addition to the securities included in the Lehman Intermediate Government/Corporate Index the following fixed income securities are also allowed:

- Passthrough mortgage-backed securities issued by Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC), and the Government National Mortgage Association (GNMA) are eligible investments. Asset or mortgage backed securities must have a minimum "AAA" rating by S&P or "Aaa" by Moody's (or equivalent ratings by other national rating services).

- Collateralized mortgage obligations (CMO's) issued by one of the above listed federal agencies (FNMA, FHLMC or GNMA) are allowable securities. At the time of purchase, these securities must not exceed the maximum allowable Flow Uncertainty Index score (FLUX) qualifications as established by the National Association of Insurance Commissioners.

F. Foreign fixed income securities are limited to government securities or equivalent.

G. Miscellaneous
- The EFIB may approve the use of financial index futures and options in order to adjust the overall effective asset allocation of the entire portfolio and for use as hedges. For example, covered call options may be used to mitigate an expected decline in securities' prices. However, futures and options positions are not meant to be used for speculation, and the EFIB must specifically approve the program for each type of use. See the prohibited investments listed below. Monies received from the sale of covered calls will be accounted for as gains and losses and combined with gains or losses on other securities. No long or short futures, or options positions may be established unless the portfolio has sufficient cash reserves or securities to either fund purchase or deliver securities under the contract.

- Foreign currency contracts may be used only as hedges to currency exposure existing within the portfolio (equities or fixed income). See the prohibited investments listed below.

- The EFIB permits security lending to qualified borrowers as prescribed in the securities' lending agreement with the custodian bank.

Prohibited Investments

The following are prohibited investments or transactions:

A. Equities
- Letter stock or other unregistered securities except those exempt from SEC registration because of short maturities. Further, the use of non-marketable (or illiquid) assets such as venture capital, leveraged buyouts, private placements, hedge funds, or similar investments is also prohibited.

- Investments in equity securities of companies with a public record of less than three years of continuous operation are prohibited.

- Short sales or margin transactions are prohibited unless the EFIB has given written approval prior to the transaction.

B. Leveraged or derivative instruments

- Commodities or commodity contracts.

- Futures and option positions are to be used for hedging only, and not for speculative purposes.

C. Miscellaneous

- Foreign currency speculation or any related investment activity is prohibited.

- The natural resource revenues (land sales, mineral royalties, grazing fees, timber proceeds and other interests and leases) contributed to the permanent endowment and earnings reserve funds by the State Board of Land Commissioners act as proxies for the real estate asset categories. Therefore, the EFIB will not invest in additional real estate asset categories with the exception of purchasing facilities to house the EFIB staff.

D. Per *Idaho Code*, Section 57-715

- The permanent endowment funds will be invested according to the highest standards with securities being purchased for investment purposes only and not for speculation.

- No monies shall be invested in instruments that, due to a rise in interest rates or a decline in interest rates, would put the fund at a contractual risk of not receiving interest, or at risk that the principal would not be paid.

- Investments in inverse floaters, interest only or principal only securities, reverse repurchase agreements and other securities that could impart leverage to the portfolio or have highly unpredictable cash flows are prohibited (even if the securities pass the Flow Uncertainty Index score).

Investment Manager Responsibilities

A. In addition to this general policy statement, each Investment Manager has a specific set of policies and guidelines. These specific policies are considered a part of this Investment Policy Statement. The Investment Manager(s) are required to comply with both the general and specific policies and guidelines outlined herein or as stated in any written updates. These specific policies and guidelines include a detailed description of the performance expectations for each Investment Manager.

B. The Investment Manager(s) are responsible for making all investment decisions on a discretionary basis and will be responsible for achieving the investment objectives.

C. The Investment Manager(s) are responsible for properly diversifying their portfolio with respect to individual issuer, industry and economic sector, in order to reduce risk. However, the maximum investment in the securities of any one corporate issuer shall not be more than five percent (5%) of the market value of each account managed by the Investment Manager. Additional diversification guidelines for each Investment Manager shall be specified in the specific policies and guidelines for each Investment Manager.

D. The Investment Manager(s) are required to keep the EFIB informed of any major changes in the firm's investment philosophy, any organizational or staffing changes, any management style changes (or drift), any material legal or regulatory agency proceedings affecting the firm and any material changes in the firm's financial condition within 30 days of occurrence.

E. The EFIB requires timely monthly reports of the holdings, the transactions and the total returns achieved from the Investment Managers. The Investment Managers (or the Advisor/Consultant) shall also provide timely quarterly reports that provide additional detail on the investment strategy, outlook and performance attribution for the prior quarter. The quarterly reports must also summarize whether the portfolio is in compliance with the guidelines or state what steps are being done to correct any failures to comply.

F. All transactions should be entered into on the basis of best execution, which means the best realized net price.

G. The Investment Manager(s) are required to acknowledge in writing their acceptance of fiduciary responsibility under all legislation (including Idaho's Uniform Prudent Investor Act) and be registered under the Investment Advisory Act of 1940.

Advisor/Consultant's Responsibilities

A. The Advisor/Consultant will prepare and deliver a quantitative review of the portfolio on a quarterly basis. This review will include a summary of the EFIB's assets and report on their investment performance for the most recent quarter, year-to-date and since inception of each account. Investment performance includes both periodic returns and the appropriate measurements of risk or volatility.

B. The incremental return or risk reduction provided by the EFIB's tactical asset allocation policy will be reported separately from the Investment Manager's results in the performance reporting system provided by the Advisor/Consultant. The "attribution analysis" portion of the periodic performance reports must accurately report on the asset allocation policy contribution.

C. The Advisor/Consultant will establish a benchmark objective for each Investment Manager and will compare each Investment Manager's investment performance (periodic returns and risk) with the specific benchmark objectives.

D. The Advisor/Consultant will assist the EFIB in determining the appropriate fees and expenses to be paid to the Investment Managers. The Advisor/Consultant will periodically conduct a survey to determine if the EFIB's fees, commissions and expenses are appropriate for the level of assets managed by each Investment Manager.

E. The EFIB has determined that the Advisor/Consultant's duties include periodic visits to the Investment Managers to determine if they are in compliance with the EFIB's investment policies and guidelines.

F. The EFIB is concerned that the Advisor/Consultant and the Investment Managers be as independent as possible to avoid possible conflicts of interest (or the appearance of conflicts of interest). Therefore, the EFIB requires that any and all forms of commissions, fees, expense reimbursements or other compensation (i.e., "soft dollars" or "directed trades") that may exist between the Advisor/Consultant and the Investment Managers be fully disclosed in writing to the EFIB prior to the EFIB signing a contract with the Investment Managers.

OPERATING FUNDS MANAGEMENT POLICY

Operating Funds and Non-Recurring Items

The Operating Funds include the day-to-day operating funds. Therefore, investments with a maturity of one year or less are appropriate for this segment. The amount of operating funds required in these funds is determined annually from the Sources & Uses Model. These funds are invested with the objective of preserving principal and maintaining liquidity. It is generally anticipated that the average maturity of these funds will be six (6) months.

The Non-Recurring Funds segment includes assets that are specifically identified for capital projects or other programs with fairly certain payment amounts and timing. These funds will be invested in fixed-income securities with maturity (or duration) dates that match the expected expenditure dates. These funds are invested with the objective of preserving principal and matching liquidity to specific projects and programs.

General Investment Guidelines

A. Repurchase Agreements – Repurchase Agreements may be transacted on a delivery versus payment basis and are restricted to those banks and dealers that deliver collateral to a third party for safekeeping. The collateral must be 102% of the total Repurchase Agreement transaction.

B. Ratings – All domestic corporate bonds, notes, debentures or convertible debt securities must have an S&P rating of "BBB" or higher or a Moody's rating of "Baa3" or higher (or equivalent by other national rating service). Asset or mortgage backed securities must have a minimum rating of "AAA" by S&P or "Aaa" by Moody's (or equivalent by other national rating service.

C. Diversification – The exposure of the Operating Funds and the Non-Recurring Items, separately or combined, to any single issuer (other than the US government or agencies) shall not exceed 5% of the market value of the separate funds.

Allowed Investments

The following securities are permitted in the Operating Funds and Non-Recurring Items Funds:

A. Only domestic securities are allowed in both the Operating Funds and Non-Recurring Items Funds.

B. US Government and Agency securities - Including Strips and discount securities. All zero coupon securities must have a maturity of less than one year.

C. Money Market Funds - Only money market funds whose credit quality characteristics match this policy may be used.

D. Bank Certificates of Deposit - Non-negotiable certificates of deposit and savings accounts of federally insured institutions located in the State of Idaho shall be limited to the amount resulting from computing the "Financial Institution Investment Limit Formula" approved by the EFIB.

E. Banker's Acceptances

F. Commercial Paper – Commercial paper holdings are limited to five percent (5%) of each separate fund.

G. Local Government Investment Pools

H. Asset or Mortgage-Backed Securities

I. Corporate Bonds, Notes or Debentures

J. Guaranteed Investment Contracts